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5 COMMON PROBLEM AREAS FOR COMPENSATION OF NON-EXEMPT EMPLOYEES

Despite the fact we have been living with the federal Wage & Hour Act (the Fair Labor Standards Act of 1938, as amended, 29 U.S.C. §§ 201 et. seq.) for more than seventy years, a number of issues continue to cause problems. This paper will discuss, in the context of different fact situations, a number of these problems. However, before beginning this discussion, the following is a brief overview of the applicable laws and terminology.

I. OVERVIEW OF APPLICABLE LAWS

A. Fair Labor Standards Act

The Fair Labor Standards Act of 1938, as amended, 29 U.S.C. §§ 201 et. seq. ("FLSA") requires that employers covered by the FLSA pay to their employees at least the minimum hourly wage prescribed by the FLSA ($7.25 per hour since July 24, 2009) for each hour worked and that such employers pay eligible employees at least one and one half times the employee’s regular rate for all hours worked by the employee in excess of 40 hours in a given work week. FLSA §§ 6, 7. The FLSA applies to employers with employees engaged in commerce, and the production of goods for commerce, or in the handling, selling or otherwise working on goods that have been moved in or produced for commerce, with annual gross volume of sales made or business done of $500,000.00 or more (exclusive of excise taxes at the retail level that are separately stated).

Even if the employer does not meet the $500,000.00 test, the FLSA still applies to individual employees who are engaged in interstate or foreign commerce or producing goods
for transportation in interstate or foreign commerce. The FLSA does not apply to independent contractors.

The FLSA is enforced by the United States Department of Labor, Wage and Hour Division. Additionally, individual employees are entitled to bring actions to enforce the FLSA in either federal or state court. Remedies available to individual employees include unpaid minimum wages, unpaid overtime, an additional amount up to the amount owed as liquidated damages, and attorney’s fees. The FLSA provides for the potential of a $10,000.00 fine for willful violations and imprisonment for 6 months for a repeat conviction. The FLSA also provides for a civil penalty not to exceed $10,000.00 for a child labor violation and a civil penalty not to exceed $1,000.00 for each violation of the Section 6 (minimum wage) and Section 7 (overtime) provisions of the Act.

Most FLSA audits result from individual employee complaints. In the audit process, the United States Department of Labor generally both 1) requires employers to correct non-complying policies and 2) also collects unpaid back wages and overtime on behalf of all affected employees for the period of two years preceding the audit. This two year period reflects the statute of limitations for non-willful violations. However, in the case of willful violations, the statute of limitations is three years and the Wage and Hour Division can assess back wage liabilities for this three year period.

B. **North Carolina Wage and Hour Act**

The North Carolina Wage and Hour Act ("NC Act"), §§95-25.2 et. seq. of the North Carolina General Statutes, also requires that employers pay the minimum wage specified by the FLSA (with a provision for 90% of the minimum wage for students and apprentices), requires overtime at a rate of not less than 1½ of the employee’s regular rate of pay for hours worked in
excess of 40 per week, has provisions relating to youth employment, and contains a number of specific requirements relative to the timing, conditions and methods of payment to employees. The minimum wage and overtime requirements of the NC Act generally apply to businesses not covered by the FLSA, such as business enterprises grossing less than $500,000.00 per year or businesses not engaged in interstate commerce. However, the wage payment requirements of the NC Act apply to all employers in North Carolina.

The provisions of the NC Act are enforced by the North Carolina Department of Labor, Wage and Hour Division. The NC Act also allows employees to retain their own attorneys and bring suit in North Carolina state court. In addition to unpaid amounts due, the NC Act gives the court discretion to award liquidated damages in an amount equal to the amount found to be due, plus interest from date payment should have been made, plus costs and attorney’s fees. In determining whether or not to award liquidated damages, the court can consider whether the employer had reasonable grounds for believing that the employer’s act or omission was not in violation of the NC Act. §95-25.21(a)(1). Claims under the NC Act are subject to a two year statute of limitations.

II. "TERMS OF ART/RULES"

In discussing both the FLSA and the NC Act, it is helpful to understand certain "terms of art" which have very specific meanings for purposes of application of these laws. For example, both the FLSA and the NC Act require employers to pay overtime at 1½ times an employee’s "regular rate" for all "hours worked" by the employee during a given "week".

A. "Exempt/non-exempt"

Neither the FLSA nor the NC Act recognize a distinction, for overtime purposes, based on whether the employees are "hourly" personnel or "salaried" personnel. Rather, whether an
employee must be paid overtime depends upon whether the employee is "exempt" or "non-exempt" from the requirements of the Act. Compensation of an employee on a "salary" basis is merely an element in certain of the exemptions.

B. "Work week"

All wage and hour overtime computations are performed on the basis of a single work week. A "work week" is a fixed and regularly recurring period of seven consecutive days. The work week can start on any particular day of the week, but once established, this day must remain fixed as the starting day for the work week. 29 CFR §778.105.

The FLSA does not allow averaging of hours over two or more work weeks (29 CFR §778.104). Except with respect to employees of a public agency which is a state, a political subdivision of a state, or an interstate governmental agency, employers may not substitute "comp" time (compensatory time off) for overtime payments. FLSA §§7(a)(1) and (o).

C. "Regular rate"

As noted above, for overtime purposes, employees must be paid 1½ times their "regular rate" for all hours worked in excess of 40 in any week. The "regular rate" is the hourly rate actually paid the employee for the normal, non-overtime work week for which he or she is employed. FLSA §7(e) requires inclusion in the "regular rate" of all remuneration for employment paid to, on behalf of, the employee except:

1. sums paid as gifts (amounts of which are not measured by or dependant upon hours worked, production or efficiency);

2. payments for occasional periods in which no work is performed due to vacation, holiday, illness, failure of the employer to provide sufficient work, or other similar cause, and reimbursable expenses;

3. sums paid in recognition of services if either
(a) both the fact that the payment is to be made and the amount of the payment are determined at the sole discretion of the employer and not pursuant to any arrangement causing an expectation in the employee of such payments; or

(b) the payments are made pursuant to a bona fide profit-sharing plan or trust; or

(c) the payments are talent fees paid to performers.

(4) Irrevocable contributions by an employer to a bona fide plan providing for old-age, retirement, life, accident or health insurance or similar benefits;

(5) extra compensation provided by a premium rate paid for certain hours worked in any day or work week because such hours are hours worked in excess of 8 in a day or in excess of the maximum work week applicable to such employee;

(6) extra compensation provided by a premium rate paid for work by the employee Saturdays, Sundays, holidays, etc. where such a premium rate is not less than 1½ times the rate established in good faith for like work performed in non-overtime hours on other days; or

(7) extra compensation provided by a premium rate paid to the employee pursuant to contract for work outside of hours established in good faith by the contract or agreement as the basic, normal or regular work day where such premium rate is not less than 1½ times the rate established in good faith by the contract or agreement for like work performed during such work day or work week.

Extra compensation paid as described in paragraphs (5), (6) and (7) above is creditable towards overtime compensation.

Only the above listed payments can be excluded from the regular rate. For example, if an employee receives non-cash wages such as room and board, the reasonable cost or fair value of these non-cash wages must be included in computing overtime for any week in which the non-exempt employee works more than 40 hours.

Similarly, incentive pay or production bonuses must be included for purposes of computing overtime. The Department of Labor takes the position that bonuses which are
designed to encourage increased efforts on the part of employees constitute earnings. These earnings must be included in determining the employee’s regular rate and therefore also in making overtime computations. The only bonuses which are excludable from overtime computations are discretionary bonuses, not expected or anticipated from the employee’s standpoint, which constitute a gift from the employer. Examples of bonuses which the Department of Labor contends are includable in overtime pay calculations include attendance bonuses, production bonuses, bonuses for quality and accuracy of work, efficiency bonuses, length-of-service bonuses, bonuses promised to employees at the time of hiring, and bonuses provided in contracts. Bonuses which do not have to be included for purposes of computing overtime include Christmas bonuses, gift bonuses, bonuses wholly within the employer’s discretion, profit sharing bonuses paid pursuant to profit sharing plans and trusts, and bonuses based on a percentage of an employee’s total wages. With respect to the Christmas bonuses, the bonus may be paid with such regularity that the employees expect it and the bonus may vary for different employees on the basis of salary, hourly rate, or length of service. However, the bonus must not be measured by hours worked, production or efficiency; the bonus must not be so substantial that the employees consider it a part of their wages; and the bonus must not be paid pursuant to a contract.

Where a bonus includable in the regular rate is earned for a specific weekly pay period in which the employee worked overtime, compensation for that week is computed by multiplying the employee's regular hourly rate by the total number of hours worked to obtain his straight time earnings. The bonus is then added to these straight time earnings and that figure is divided by the total number of hours worked to obtain the regular hourly rate for overtime purposes. One half of this figure is then multiplied by the number of overtime hours.
The sum of the straight time hours, plus the bonus, plus the overtime, equal the total compensation owed to the employee for the week in question.

Where a bonus includable in the regular rate cannot be computed for a given work week, the employer may temporarily disregard the bonus in computation of the regular rate and apportion the bonus back over the work week in which it was earned at such time as the bonus can be calculated. The employee must then be paid an additional amount equal to one-half the hourly rate of pay allocable to the bonus for the weeks in question.

D. “Hours worked”

"Hours worked" includes not only time spent by employees actually performing work, but also, depending upon the circumstances, travel time, (29 CFR §785.33), waiting time (29 CFR §785.14), on-call time (§785.17), and training time (§ 785.27).

(1) Travel time

Under the Portal-to-Portal Act, travel by an employee from the employee's home to the worksite and travel from the worksite to the employee’s home after work does not constitute "hours worked" and is therefore not compensable where overnight travel away from the employee’s home community is not involved. 29 C.F.R. §785.35. However, travel during the course of a day's work as part of the employee’s principal activity, such as travel from jobsite to jobsite, must be counted as hours worked. 29 C.F.R. §785.38. If, after returning home, after completing his day's work, an employee is subsequently required to go to a customer's place of business to perform work, all travel between the employee’s home and the customer's place of business is working time and must be compensated. As an enforcement policy, where, after an employee’s normal business day, the employee is required to return to the
employer’s place of business (rather than a customer’s place of business), the Department of Labor does not require the travel time to be considered as hours worked. 29 C.F.R. §785.36.

However, the Portal-to-Portal rules concerning non-compensability of travel time between home and work change where an employee is either away from home on work on a special one day assignment to another city or the employee is required to travel away from the employee’s home community overnight. Where an employee who regularly works at a fixed location in one city is given a special one day work assignment in another city, time spent by the employee traveling to and from the special assignment will be counted as hours worked and must be compensated. The Wage and Hour Division considers operation of an automobile to be "work" and, therefore, hours spent in operating an automobile to and from a special assignment as compensable. However, if the employer offers public transportation (air, rail, bus, etc.) to the employee but the employee nevertheless wishes to operate his or her automobile instead, the employer may count as hours worked either the time spent driving the car or the time the employer would have had to count as hours worked during working hours if the employee had used the public conveyance. 29 C.F.R. §785.40.

In the case of a special one-day assignment, where an employer offers to provide public transportation, the employer would not be required to count as hours worked either the travel between the employee’s home and the public transportation or the employee’s usual meal time. However, hours actually spent traveling on the public transportation, both before, during and after regular working hours, would have to be treated as hours worked. 29 C.F.R. §785.37.

Where travel takes an employee away from home overnight, such travel is considered to be hours worked when it occurs during regular working hours, regardless of whether the travel occurs during the week day or during corresponding hours on non-working days.
Regular meal period time can be deducted. As an enforcement policy, the Division will not consider as work time any time spent in travel away from home outside of regular working hours when the employee is a passenger. However, absent offer of public transportation by the employer, even time spent outside of normal working hours would be counted as hours worked, and therefore would be compensable, where an employee drives an automobile. 29 C.F.R. §785.39.

(2) "On call" and "waiting" time

Under the regulations, the issue of whether time spent while waiting or while on call must be counted as hours worked turns on whether the employee is able to use the time in question effectively for his or her own purposes. 29 CFR §785.15.

(3) Lectures, Meetings, and Training Programs

In 29 CFR §§785.27 through .31, the Department of Labor has set up four tests which an employer must meet in order to justify not compensating employees for time spent in lectures, meetings, and training programs. Additionally, as discussed below, the Department of Labor has established an exception to the third test.

The four tests which must be met if time spent by an employee in training is not to be counted as hours worked are as follows:

1. Time spent in the meetings or training must be outside of the employee's regular working hours;

2. Time spent by the employee in training must be in fact voluntary (such time would not be voluntary if it is required by the employer; such time is also not voluntary if in fact the employee is given to understand or led to believe that the employee's present working conditions or the continuance of employment would be adversely affected by non-attendance);
3. The training is not directly related to the employee’s job (the training is
directly related to the employee’s job if it is designed to make the employee
handle his or her job more effectively as distinguished from training the
employee for another job or a promotion - the Wage and Hour Division gives by
way of example of training directly related to an employee’s job a stenographer
who is given a course in stenography in order to make her a better stenographer.
Such time would be considered hours worked (and therefore compensable).
However, if the stenographer was taking a course in bookkeeping for the
purpose of preparing for advancement through upgrading to a higher skill, such
training would not be considered hours worked); and

4. The employee does not perform any productive work for the employer
during such attendance.

The exception to the third test is that, as set forth in §785.31, an employer can offer
lectures, training sessions and courses of instruction for the benefit of his employees and not
count time spent by employees in these sessions as hours worked if the training provided by the
employer is also available to the employee through “independent bona fide institutions of
learning” such as trade schools, community colleges, universities, etc. Voluntary attendance
by an employee at such courses outside of working hours would not be hours worked even if
the instruction is directly related to the employee’s job. That is, an employer can make
available (but not require attendance at) an after-hours seminar designed to improve the skills
of the employees without incurring liability for hours worked if the seminar covers material
otherwise available to the employee through other recognized sources of instruction.

III. EXAMPLES

A. Work Week

1. A company pays its employees every two weeks, for work performed during the
preceding two weeks. If an employee works more than 80 hours during the two week period,
the company, at the employee’s option, either pays the employee overtime at the rate of 1½
times the employee’s hourly rate for the time worked in excess of 80 hours during the two week period or keeps track of the overtime and allows the employee to take this time as paid time off in the future. Do these practices create any problems?

2. If a non-exempt employee earning $10.00 an hour works 38 hours in the first week of a two week pay period and 42 hours in the second week, for a total of 80 hours in the period, what is her compensation?

3. If the employer had been averaging work weeks and paying straight $10.00 an hour for all hours worked (i.e., $800.00 for the two week period), what would the employer owe for back pay for this 2 week period?

4. If the employer had allowed the employee to “bank” the 2 hours from the second week and take time off with pay in the future, what, if anything, would the employer owe for this 2 hours?

B. Regular Rate/Bonuses

1. The company pays production incentive bonuses and has a policy of paying double time for holiday work. How if at all do such payments affect the rate at which overtime is computed?

2. If a non-exempt employee who works for $10.00 an hour worked 45 hours (9 hours each day, Monday through Friday) during a certain week in which he also earns a $50.00 production bonus, how would the bonus affect the employee’s compensation for the week.

C. Travel Time

To complete an out of town assignment, a non-exempt employee who usually works 8 to 5 with an hour for lunch drove his car to Atlanta, leaving from home at 6:00 am on Friday,
arriving in Atlanta at noon for a 2:00 pm meeting. He completed the meeting at 5:00 pm, spent the night, and drove home on Saturday, leaving at 7:00 am and arriving at 1:00 pm. His employer had offered to purchase a flight, which would have left the airport at 7:00 am Friday morning and returned Friday evening at 7:00 pm. What are the hours worked?

D. On call/Waiting Time

Is the non-exempt employee entitled to be paid for the time between his arrival at 11:00 am and the meeting at 2:00?

E. Lectures, Meetings and Training

Are you entitled to compensation for the time you spend attending this presentation?
IV. ANSWERS

A. Work Week

The company’s practice of averaging work weeks over a two week pay period violates the FLSA, as does the company’s “comp time” practice. In the event these practices are challenged, either by an employee (or former employee) or by the Wage & Hour Division, to the extent any non-exempt employee compensated on an hourly basis has worked more than 40 hours in any one week, the company will owe additional compensation in the amount of 1½ the employee’s regular rate for all hours worked by such employees in excess of 40 per week for the preceding two years.

In computing an employee’s pay, the employer must make overtime determinations on a week by week basis. If a non-exempt employee earning $10.00 an hour works 38 hours in the first week of a two week pay period and 42 hours in the second week, for a total of 80 hours in the period, the employee is entitled to gross wages for the period of $810.00 (38 hours x $10.00 [$380.00] + 40 hours x $10.00 [$400.00] + 2 hours x (1.5 x $10.00) [$30.00]). If the employer had been averaging work weeks and paying straight $10.00 an hour for all hours worked (i.e., $800.00 for the two week period), this failure to pay two hours overtime during one of the two weeks would result in a back wage assessment of $10.00 (the unpaid ½ time premium of $5.00 x 2 hours). If this mistake occurred every pay period for the preceding two years and affected 25 employees, the employer would face a back wage assessment of $6,500.00 (26 pay periods x $10.00 x 25 employees).

If the employer had allowed the employee to “bank” the 2 hours from the second week and take time off with pay in the future, the Wage & Hour Division would assess back wage liability at the full 1½ the regular rate since the employee was not paid for the 2 hours at the employee’s regular rate. The employee would have received pay for the two week period in the amount of $780.00 ($380.00 for 38 hours and $400.00 for 40 hours). The back wage liability would be $30.00 (1.5 x $10.00 x 2 hours). If the same practice had taken place with 25 other employees, the back wage assessment would be $19,500.00. If the employer had paid the employee for the two hours by the time the unpaid overtime became an issue, as an enforcement practice, the Wage & Hour Division would probably credit the employer with the “straight time” payments, even though this “paid time off” does not fall within one of the exceptions to inclusions to the “regular rate” as discussed below.

B. Regular Rate

Unless the production bonus is paid as a percentage of weekly earnings (which would automatically include overtime), the employer would have to compute a non-exempt employee’s regular rate on a weekly basis to include the production bonus for purposes of computing overtime owed for that week. If a non-exempt employee who works for $10.00 an hour worked 45 hours (9 hours each day, Monday through Friday) during a certain week in which he also earns a $50.00 production bonus, the bonus would have to be considered in computing the employee’s regular rate for the week.
To determine the "regular rate" the employer must first determine the employee’s straight time earnings for the week in question, here $500.00 (45 hours x $10.00 [$450.00]+ $50.00). The employer would then divide the straight time earnings [$500.00] by the number of hours worked [45] to obtain the regular rate for this week [$11.11 per hour]. The employer would then compute overtime liability for this week as an additional ½ of the newly computed regular rate [$5.56 per hour], multiply this premium by the number of overtime hours [5] and add this overtime premium [$27.80] to the straight time earnings of $500.00, for total gross pay for the week of $527.80.

If the employee had worked 3 of the overtime hours on a holiday pursuant to a company policy of paying double time for holiday work, the employer would not have to take the double time premium into consideration in computing the regular rate. Since the double time premium for Saturday work falls within one of the statutory exemptions mentioned above [FLSA §7(e)(6)], the double time premium does not need to be included in the computation of the regular rate. The employer could take credit for the $30 premium against the overtime liability. Since the double time premium of $30.00 exceeded the overtime liability of $27.50, the gross wages would be $530 ($500 + 3 hours x the $10.00 premium for Saturday work).

C. Travel Time

Since the employer offered public transportation that would have allowed the assignment to be completed in one day, at the employer’s option, the hours worked could include either all time from departure to return to the airport, excluding a meal period (i.e., 11 hours) or all driving time (12 hours) and the hours worked in Atlanta from arrival to 5:00 pm.

To reduce the expense to the company incident to paying an employee’s high regular wage for travel time, prospectively, an employer and employee can agree to compensate travel time at a different hourly rate, so long as the agreed upon rate is at least the prevailing minimum wage. Time spent in travel time must be included for overtime computations. Where a different rate has been agreed upon for travel time, the employer computes overtime liability for a week involving travel time by first computing total compensation due the employee for hours worked (number of hours worked by the employee at the employee’s regular rate plus the number of hours worked by the employee traveling at the travel time rate). This sum is then divided by total hours worked in that week to obtain the blended regular rate per hour. This blended regular rate per hour is then divided by two to obtain a figure for half time. This half time figure is then multiplied by the number of hours worked in excess of 40 during the week and added to the sum of the employee’s regular compensation for the week. 29 C.F.R. §778.115. For example:

An employee making $15.00 per hour works a total of 56 hours in a given week, 42 hours performing his regular duties and 14 hours travel time at a pre-agreed upon rate of $7.25 per hour. The employee’s regular rate for the week in question is the weighted average, here $13.06 per hour:
42 hours x $15.00 = $ 630.00
14 hours x $7.25 =  $ 101.50
$ 731.50

$731.50 divided by 56 hours = $ 13.06 per hour

Overtime liability would be \( \frac{1}{2} \) of $13.06 per hour ($6.53 per hour) x the number of overtime hours (16), for a total of $104.48. Total compensation due for the week would be $835.98 ($731.50 + 104.48).

By contrast, if the 14 hours travel time had been paid at the employee’s normal rate of $15.00 per hour, overtime liability would be $360.00 (1.5 x $15.00 x 16 hours), and total compensation due the employee would be $960.00 ((40 hours x $15.00 per hour) + (16 hours x $22.50 per hour)).

D. **On Call or Waiting Time**

If he is free pursue his own interests without restrictions (use the time effectively for his own purposes” 29 CFR §785.17), the time between his arrival and commencement of the meeting will not be considered hours worked.

E. **Lectures, Meetings and Training Programs**

- Is it outside your regular working hours?
- Is it voluntary
- Is it directly related to your job (i.e., designed to make you handle your job more effectively)? [Note cases like Price v. Tampa Electric Co and Chao v. Akron Insulation]
- Have you performed any productive work for your employer while attending?